Supreme Court, U.S.
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No. 95-195

In The

Supreme Court of the United States

October Term, 1995

L. B. WINDHAM, *et al.*,

Petitioners,

vs.

FIRST GIBRALTAR BANK, F.S.B.,

Respondent.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

Oklahoma, by statute, prohibited default rent assignments as additional security for debt secured by mortgages on real property. Under state law, such assignments neither transferred an interest in rent to a mortgagee nor created a security interest in rental income. The questions presented relate to the unwillingness of the United States Court of Appeals for the Tenth Circuit, in the context of a bankruptcy, to follow Oklahoma's clear statutory scheme and are as follows:

1. Does the refusal of the Tenth Circuit Court of Appeals to re-examine the issues in *Virginia Beach Federal Savings and Loan Ass'n. v. Wood,* 901 F.2d 849 (10th Cir. 1990), in light of Oklahoma law contrary to that decision, invade the rights reserved to the sovereign States under the Tenth Amendment and extend federalism beyond the contemplation of the *Erie* doctrine, particularly: (a) May federal courts fashion an equitable remedy based upon pre-*Erie* federal common law to permit creation of liens on rents by judicial fiat in contravention of Oklahoma law; and, (b) May the Tenth Circuit disregard Oklahoma statutory prohibitions against restraint of the right of redemption to recognize an equitable lien *qua* security interest, in rents in bankruptcy, after the mandate of *Butner v. United States*, 440 U.S. 48 (1979); and,

2. Whether the Tenth Amendment and principles of federalism should be interpreted to require federal courts of appeal, when reviewing district court interpretations of state law *de novo* under *Salve Regina College v. Russell,* 449 U.S. 225 (1991), to expressly state in any opinion rendered *either* that the court has examined state law and believes the applicable state law is settled and certification of the question to the state's highest court is unnecessary *or* that, because of uncertainty as the applicable state law, certification of the question to the state's highest court is required.

PARTIES TO THE PROCEEDINGS

Additional Petitioners in the caption of the case in this Court include: John J. Plotnik; Fred A. Sheriff; Jay W. Lorch; John H. Lindsey; Dale B. Elmore; C. Jackson Grayson, Jr.; Douglas A. Dawson; Peter L. Marr; Hanaho Ltd., a Texas general partnership consisting of John J. Redfern, Roberta Garst, and Rosalyn Grover; W. E. Penland; and, Eagle Texas Realty Company, Inc.

The caption of the case does not contain the names of all the parties appearing in the United States Court of Appeals for the Tenth Circuit. The parties in the circuit court were the bankruptcy debtor, OKC Partners, Ltd., also known as Town & Country/ Courtyard Plaza, a Texas limited partnership; Michael B. Birnie, a representative creditor; Appellants L. B. Windham; John J. Plotnik; Fred A. Sheriff; Jay W. Lorch; John H. Lindsey; Dale B. Elmore; C. Jackson Grayson, Jr.; Douglas A. Dawson; Peter Marr; Hanaho, Ltd.; John J. Redfern, III; William E. Penland; Eagle-Texas Realty Company, Inc.; Appellees OKC Partners, Ltd.; First Gibraltar Bank F.S.B.; and, Appellees in district court only, Lipscomb Norvell, Jr. and Blockbuster Video.

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Petitioners, L B. Windham, *et al.*, respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Tenth Circuit.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Tenth Circuit (Appendix "B", *infra*) is unreported and is based upon, and affirms, the opinion of the United States District Court for the Western District of Oklahoma (Appendix "C", *infra*).

STATEMENT OF JURISDICTION

The United States Court of Appeals for the Tenth Circuit entered its judgment on May 4, 1995. On June 6, 1995, that court denied a petition for rehearing with a suggestion for rehearing in banc (Appendix "A", *infra).* The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

Amendment X - Reserved Powers to States.

> The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people.

11 U.S. C. § 363(a) Use, sale, or lease of property

> (a) In this section, "cash collateral" means cash, negotiable instruments, documents of title, securities, deposit accounts, or other cash equivalents whenever acquired in which the estate and an entity other than the estate have an interest and includes the proceeds, products, offspring, rents, or profits of

property subject to a security interest as provided in section 552(b) of this title, whether existing before or after the commencement of a case under this title. (Pub.L. 95-598, Nov. 6, 1978, 92 Stat. 2572; Pub.L. 98-353, Title III, § 442, July 10, 1984, 98 Stat. 371; Pub.L. 99-554, Title II, § 257(k), Oct. 27, 1986, 100 Stat. 3115.)

11 U.S.C. § 552(b) Postpetition effect of security interest.

(b) Except as provided in sections 363, 506(c), 522, 544, 545, 547, and 548 of this title, if the debtor and an entity entered into a security agreement before the commencement of the case and if the security interest created by such secuity agreement extends to property of the debtor acquired before the commencement of the case and to proceeds, product, offspring, rents, or profits of such property, then such security interest extends to such proceeds, product, offspring, rents, or profits acquired by the estate after the commencement of the case to the extent provided by such security agreement and by applicable nonbankruptcy law, except to any extent that the court, after notice and a hearing and based on the equities of the case, orders otherwise. (Pub.L. 95-598, Nov. 6, 1978, 92 Stat. 2602; Pub.L. 98-353, Title III, § 466, July 10, 1984, 98 Stat. 380.)

STATEMENT OF THE CASE

This Petition raises fundamental questions of federalism and concerns the relationship between the sovereign State and federal courts, and the obligation of federal courts to apply state law in

certain circumstances. In sum, this case relates to the different treatment of a putative security interest in rental income, which is governed entirely by state law,[1] as between state courts and federal courts in Oklahoma.

The Petitioners are limited partners and the general partner of OKC Partners, Ltd., a Texas limited partnership ("the Partnership"). The Partnership owned two shopping centers in Oklahoma City, Oklahoma, known as the Town & Country Shopping Center ("Town & Country") and Courtyard Plaza Shopping Center ("Courtyard Plaza"). Both Town & Country and Courtyard Plaza were subject to mortgages in favor of First Texas Savings Association ("First Texas"), which mortgages contained provisions purporting to create an assignment of the rental income from the shopping centers in favor of First Texas, based upon default by the Partnership of its payment obligations. When the mortgages were executed, Oklahoma law did not permit a mortgage with assignment of rents as additional security for the debt secured by the mortgaged real property, if the assignment and security interest were conditioned upon future default by the mortgagor.[2] The First Texas rent assignments were, at all times,

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1. It is important to note that this case presents no issue of competing state and federal regulation of real property and, hence, no conflict between the Commerce Clause and the Tenth Amendment is present.

2. Title 46 O.S. Supp. 1979, § 4 provides:

> Every instrument substantially the same as the above shall be deemed a good and valid mortgage, with all contracts and covenants essential to protect the rights of the holder thereof; but any further lawful contract embodied therein shall be binding upon the parties thereto; and when the words, "and waive the appraisement" are written or printed therein, the premises mortgaged must be sold without appraisement, in case of foreclosure and sale

(Cont'd)

void under Oklahoma law since any security interest would vest only after "default by the mortgagor."

(Cont'd)

> thereunder, and in such case no order for such sale shall issue for six (6) months after the date of judgment; likewise *nothing in this title or in Sections 10 and 11 of Title 42 of the Oklahoma Statutes, shall be construed to prevent a mortgagor,* in a mortgage transaction not involving a consumer loan or a consumer related loan as said terms are defined in Sections 3-104 and 3-603 of Title 14A of the Oklahoma Statutes, *from mortgaging and assigning the rents and profits from the mortgaged real property as additional security for the debts secured by the mortgage, where such assignment* (i) is made contemporaneously with the execution of the mortgage, either as a provision therein or by separate instrument, and (ii) covers a lease or leases then existing or thereafter executed, including renewals or extension thereof or substitutes therefor, which cover all or any part of the mortgaged real property, and (iii) *is an assignment not conditioned upon a future default by the mortgagor,* and (iv) provides for the immediate collection by the mortgagee, or its successors, assigns or agents, of the rents and profits so assigned as the same become due. Any mortgagee taking an assignment of rents and profits as described above shall have the obligation to account and pay to the mortgagor regarding any rents and profits actually collected pursuant to such assignment, which are not applied on the indebtedness owning to the mortgagee; however, the mortgagee shall not be deemed to have other fiduciary obligations to the mortgagor resulting from such assignment or be deemed to be in possession of the mortgaged real property, unless the mortgagee also enters into continued physical possession of the mortgaged real property and exercises exclusive operating control of the mortgaged real property. [Emphasis added.]

On March 30, 1988, First Texas initiated a foreclosure proceeding in an Oklahoma state court against the Partnership seeking, *inter alia,* the appointment of a receiver. On May 24, 1988, the Partnership filed a petition under Chapter 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the Western District of Oklahoma ("the Bankruptcy Court"). After First Texas filed a motion in the Bankruptcy Court to prohibit the use of cash collateral and to modify the automatic stay, the limited partners challenged the claim of First Texas to a security interest in the rents. The central issue was whether, under "applicable non-bankruptcy law [state law]," First Texas had a lien on the rents that was protected under 11 U.S.C. §§ 363(a) and 552(b).[3] Hence, the gravamen of the First Texas motion in the Bankruptcy Court was that it was entitled to post-petition rents from both shopping centers under the assignment of rents clauses contained in the mortgages. After First Texas was declared insolvent, the notes and mortgages were acquired by Respondent, First Gibraltar Bank, F.S.B. ("Gibraltar").

The parties submitted briefs to the Bankruptcy Court as to whether, under Oklahoma law, the rental income was subject to a security interest in favor of Gibraltar. However, shortly before the Bankruptcy Court was prepared to issue its opinion on the rental issue, the United States Court of Appeals for the Tenth Circuit issued its decision in an unrelated case, *Virginia Beach Federal Savings and Loan Ass'n. v. Wood,* 901 F.2d 849 (10th Cir. 1990) (Appendix "D", *infra*), which decision recognized the execution of a mortgage as creating an equitable lien *qua* security interest in rents under Oklahoma law, and which was, in fact, contrary to Oklahoma law.

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3. The basis for jurisdiction in the Bankruptcy Court is 28 U.S.C. § 157 and, with respect to appeals to the district court and the court of appeals, 28 U.S.C §§ 158(a) and (d), respectively.

Based upon *Virginia Beach*, the Bankruptcy Court issued a two paragraph opinion finding *Virginia Beach* controlling. Petitioners appealed the Bankruptcy Court's decision (after two modifications by the Bankruptcy Court) to the United States District Court for the Western District of Oklahoma which also found *Virginia Beach* controlling. Petitioners then appealed to the United States Court of Appeals for the Tenth Circuit which, in a one paragraph opinion, found *Virginia Beach* controlling and affirmed the district court for the reasons stated in the district court's opinion. The court of appeals opinion does not mention *de novo* review and makes no findings as to the applicable state law.

REASON FOR GRANTING THE WRIT

I.

VIRGINIA BEACH AND THE DECISION OF THE COURT OF APPEALS HEREIN FAILED TO APPLY OKLAHOMA LAW AS REQUIRED UNDER THE *ERIE* DOCTRINE AND, THUS, IMPROPERLY USURP OKLAHOMA'S RIGHT TO REGULATE REAL PROPERTY RIGHTS.

Virginia Beach relies solely upon a pre-*Erie* case, *Little v. Keaton*, 38 F.2d 457 (10th Cir. 1930), *cert. denied*, 282 U.S. 847 (1930), as its authority to justify the creation in bankruptcy of a security interest in rents *void under Oklahoma law.* 46 O.S. Supp. 1979, § 4. By reliance on *Little*, the Tenth Circuit reverts back to the doctrine of *Swift v. Tyson*, 41 U.S. (16 Pet.) 1 (1842), and ignores the mandate of this Court in *Erie R. Co. v. Tompkins*, 304 U.S. 64 (1938).

The decision of the court of appeals must be reversed because of the importance of the question of whether a federal court is free to disregard established Oklahoma law prohibiting creation of such security interest to fashion an equitable remedy

based solely upon federal common law.[4] This Court should re-evaluate the propriety of the federal judiciary's exercise of power to create a remedy contrary to Oklahoma law. This extension of federal judicial power is just as pernicious to the appropriate balance of federal and state powers as is an excess of legislation by the Congress to intrude upon the sovereign rights reserved to the States. The federal judiciary, as one branch of government, has no greater right to intrude upon the authority of the several States than does the legislative or executive branch. "Each State in the Union is sovereign as to all the powers reserved. It must necessarily be so, because the United States have no claim to authority but such as the States have surrendered to them." *Chisholm v. Georgia,* 2 U.S. (2 Dall.) 419, 435 (1793), (Iredell, J.).

As Justice Kennedy stated in his concurring opinion with Justice O'Connor in *United States v. Lopez*, 115 S. Ct. 1624, 1639 (1995),

> [T]he federal balance is too essential a part of our constitutional structure and plays too vital a role in securing freedom for us to admit inability to intervene when one or the other level of Government[5] has tipped the scales too far.
>
> In the past this Court has participated in maintaining the federal balance through judicial exposition of doctrines such as * * * the rules for determining the primacy of state

4. Petitioners note that they have repeatedly sought, to no avail, certification of the rental issue by the federal courts to the Oklahoma Supreme Court.

5. Petitioners presume that "Government" encompasses the judicial branch.

> law, *see, e.g., Erie R. Co. v. Tompkins* . . . [remaining citations omitted.]

Throughout *Virginia Beach*, the judicial branch has reached behind *Erie* to judicially fashion a remedy, ignoring the primacy of state law, despite the fact that *Erie* cautions:

> There is no federal general common law. Congress has no power to declare substantive rules of common law applicable in a state whether they be local in their nature or "general," be they commercial law or a part of the law of torts. And no clause in the Constitution purports to confer such a power upon the federal courts.

304 U.S. at 78.

The federal general common law relied upon by the *Virginia Beach* court was extracted from 41 C.J. 628.[6] Applying the "general rule in such cases," the *Virginia Beach* court, citing *Little*, states: "the [receiver] statute recognizes the mortgage as creating an equitable lien on the rents pending foreclosure." 901 F.2d at 851. Yet neither *Little* nor *Virginia Beach* cite *Oklahoma* authority for this interpretation of the Oklahoma receiver statute, 12 O.S. 1991, § 1551.

Next, to perfect this equitable lien in Oklahoma, *Virginia Beach* relies upon 51 Am. Jur. 2d *Liens* § 22 (1970), a general

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6. This general rule from Corpus Juris, cited by the court as set forth above, was later rejected by the Oklahoma Supreme Court in *Hart v. Bingman*, 171 Okl. 428, 43 P.2d 447 (1935) and *Rives v. Mincks Hotel Co.*, 167 Okla. 500, 30 P.2d 911 (1934). Since *Hart* and *Rives*, decided *after Little*, articulate the public policy prohibitions against assignments of rent, *Little* has never had any effect on Oklahoma law. The "general rule" applied by the Tenth Circuit has never been followed. *Little* has *never* been cited as authority by an Oklahoma court for the legal principle articulated in *Virginia Beach*.

discussion of equitable liens. This treatise recognizes that "in order to give rise to an equitable lien there must be an intent . . . that the property [*i.e.*, rents] serve as security for the payment of the debt. . . ." In the instant matter no such intent could be given effect, since such transaction was contrary to public policy and void in Oklahoma. 15 O.S. 1991, §§ 211, 212. No amount of federal common law or general legal principles can correct this infirmity. The federal judiciary may not override the established public policies of the sovereign State to create an equitable remedy long repudiated by Oklahoma's legislature and its Supreme Court.

Oklahoma courts have substantially limited the effect of the receiver's statute, noting that receivership is not a substantive right, but rather is ancillary to equitable relief and a provisional remedy. *Oklahoma Company v. O'Neil*, 440 P.2d 978 (Okl. 1968). Using the receiver statute, as the circuit has, as the basis for an equitable lien on rents gives a mortgagee a substantive right unavailable in Oklahoma at the time these mortgages were executed.[7] As Justice Brandeis reasoned in *Pusey & Jones Company v. Hanssen*, 261 U.S. 491, 497 (1923):

> A receiver is often appointed upon application of a secured creditor who fears that his security will be wasted. * * * But an unsecured simple contract creditor has, in the absence of statute, no substantive right, legal or equitable, in or to the property of his debtor. This is true, whatever the nature of the

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7. The *Erie* doctrine constrains "whatever inherent equitable and remedial powers federal courts possess and . . . dictates that remedies for state-created rights be granted according to state law. Rights and remedies are closely interrelated concepts; to deviate from the state's definition of the latter often would change the former as well." Wright, Miller & Cooper, *Federal Practice and Procedure: The Erie Doctrine* § 4513 (West 1982).

> property, and although the debtor is . . . insolvent. The only substantive right of a simple contract creditor is to have his debt paid in due course. * * * A receivership is not final relief. The appointment determines no substantive right, nor is it a step in the determination of such a right. [Citations omitted.]

Virginia Beach propels the receiver statute beyond legislative contemplation. It uses the same statute to create and perfect the equitable lien that *Virginia Beach* "recognizes" under *Little*. *Virginia Beach* does not inquire as to whether Oklahoma decisions followed the general rule articulated in *Little*. In fact, Oklahoma decisions do not.

II.

THE TENTH AMENDMENT AND THE *ERIE* DOCTRINE DO NOT PERMIT A FEDERAL COURT TO DISREGARD ESTABLISHED STATE LAW AND SHOULD BE INTERPRETED TO REQUIRE COURTS OF APPEAL TO EXAMINE STATE LAW *DE NOVO* AND STATE IN ANY OPINION WHETHER STATE LAW IS SUFFICIENTLY SETTLED OR WHETHER CERTIFICATION OF THE QUESTION TO THE STATE'S HIGHEST COURT IS NECESSARY.

Petitioners did not receive a *de novo* review of applicable Oklahoma law by any federal court. All relied on *Virginia Beach* without meaningful comment or review respecting the actual controlling state law.[8] Thus, Petitioners were, by a process devoid

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8. The bankruptcy and district courts were constrained to follow *Virginia Beach* as circuit precedent and the three judge panel of the court of (Cont'd)

of any substantive review of state law, denied rights emanating from the *Erie* doctrine and from the reservation of certain powers to the States by the Tenth Amendment, particularly the right to have simple real property issues decided uniformly under state law.

A recent decision of this Court demonstrates the continuing importance of the *Erie* doctrine. In *Salve Regina College v. Russell,* 499 U.S. 225, 239 (1991), this Court held that federal courts of appeal, under "principles of a cooperative judicial federalism underlying Erie," review the state-law decisions (*i.e.,* interpretations) of district courts *de novo.*[9] Petitioners seek merely an extension of *Salve Regina College* by requiring, as part of the *de novo* review, that courts of appeal simply respect state law by stating in any opinion rendered *either* that the court has examined state law and believes that the applicable state law is settled and that certification of the question to the state's highest court is unnecessary, *or* that because of uncertainty as to the applicable state law, certification of the question to the state's

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appeals was likewise required to follow *Virginia Beach* as controlling. Hence, no review of Oklahoma law was ever conducted. Moreover, the *Virginia Beach* appellants did not raise the *Erie* doctrine arguments asserted by these Petitioners.

9. Citing *Hanna v. Plumer,* 380 U.S. 460, 468 (1965), the *Salve Regina College* Court indicated that the "twin aims of the Erie doctrine [are] 'discouragement of forum-shopping and avoidance of inequitable administration of the laws. . . .' " *Salve Regina College,* 499 U.S. at 234. *Accord, Chambers v. Nasco, Inc.,* 501 U.S. 32, 52 (1991). *Virginia Beach* has created both the potential for forum shopping and an inequitable administration of the laws. Thus a creditor who is unsecured in state court becomes secured in bankruptcy. Moreover, because of *stare decisis* and court of appeals rules limiting review of panel decisions, Petitioners have been denied any review whatsoever of applicable Oklahoma law by the federal courts.

highest court is required. This is a minor burden for the courts compared to the stress placed on our federal system when federal courts disregard state law and base decisions upon federal precedent inharmonious with actual state law.

In *Fry v. United States*, 421 U.S. 542, 547-8, n. 7, (1974),[10] the Court referred to the Tenth Amendment as follows:

> Petitioners have stated their argument, not in terms of the Commerce power, but in terms of the limitations on that power imposed by the Tenth Amendment. While the Tenth Amendment has been characterized as a "truism," stating merely that "all is retained which has not been surrendered," *United States v. Darby*, 312 U.S. 100, 124 (1941), it is not without significance. The Amendment expressly declares the constitutional policy that Congress may not exercise power in a fashion that impairs the States' integrity or their ability to function effectively in a federal system.

Unlike *Fry*, there is no conflict here between the Commerce

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10. The instant case is somewhat unique in Tenth Amendment jurisprudence. Petitioners merely seek a mechanism to ensure that federal appellate courts endeavor to follow controlling state law. Many Tenth Amendment cases pertain to conflicts between Congressional power under the Commerce Clause and the reservation of certain state rights under the Tenth Amendment. *Fry, supra.* The ability of Congress to direct the states to regulate a particular field has also been decided. *New York v. United States*, 505 U.S. 144 (1992). In contrast, Petitioners seek not to resolve a state versus federal conflict as to whose law controls but only to impose a methodical review by the appellate courts, to do, in effect, that which *Erie* compels them to do; review state law as it is presented.

Clause and the Tenth Amendment. In the instant matter, there is no federal regulation in conflict with a state function or law. The problem here is simply that the court of appeals, by refusing to review applicable Oklahoma law, has impaired Oklahoma's integrity and its ability to function in the federal system. The court of appeals decision has rendered Oklahoma law irrelevant in a circumstance where *Erie* says that Oklahoma law is controlling. The solution offered by Petitioners, and described above, is a reasonable remedy to return integrity to our dual federal and state judicial systems and should be adopted by the Court.

III.

THE FEDERAL COURT MAY NOT DISREGARD OKLAHOMA STATUTORY PROHIBITIONS AGAINST RESTRAINT OF THE RIGHT OF REDEMPTION AND RECOGNIZE AN EQUITABLE LIEN ON RENTS IN BANKRUPTCY IN LIGHT OF *BUTNER'S* MANDATE TO RESOLVE ISSUES REGARDING RENTS UNDER STATE LAW.

Oklahoma has historically guarded the rights of debtors, regarding the creation of contractual liens. By statute, a contract in restraint of the right of redemption from such lien is void. 42 O.S. 1991, §§ 10, 11.[11] While the state legislature created certain

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11. Title 42 O.S. 1991, § 10 provides:

> Notwithstanding an agreement to the contrary, a lien or a contract for a lien transfers no title to the property subject to the lien.

Title 42 O.S. 1991, § 11 provides:

> All contracts for the forfeiture of property subject to a lien, in satisfaction of the obligation secured thereby, and all contracts in restraint of the right of redemption from a lien, are void . . . .

mortgage exceptions to sections 10 and 11 of the lien statute, those exceptions are only permitted when a rent assignment is *not* based upon default. *See* note 3, *supra*. The same year that the Oklahoma legislature carved out this mortgage exception, this Court, noting that Congress has the power to fashion a uniform rule governing the extent of a mortgagee's interest in rents in a bankruptcy proceeding, also observed that when Congress has not exercised that power, the determination of property interests in a bankruptcy proceeding must be left to state law:[12]

> Property interests are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding. *Uniform treatment of property interests by both state and federal courts within a State serves to reduce uncertainty, to discourage forum shopping, and to prevent a party from receiving a "windfall merely by reason of the happenstance of bankruptcy".* [Citation omitted.]

Butner v. United States, 440 U.S. 48, 56 (1979). [Emphasis added.]

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12. Congress has recently acted to establish "uniform Laws" on the subject of certain rents and profits by amending Section 552(b) of the Bankruptcy Code to make uniform the laws regarding rents and profits from public facilities such as hotels, motels and other lodging properties by allowing security interests to extend to such rents. Congress, however, has not chosen to act to establish uniform laws on any other type of rents and profits, preferring, to have the real property law of the individual states control all other rental income. *See*, Pub. L. 103-394, Title II, § 214(a), October 22, 1994, 108 Stat. 4126.

In *Butner,* this Court adopted the rule that state law defines the security interest of the mortgagee in bankruptcy, explicitly rejecting the notion that any federal rule of equity automatically gives a mortgagee a post-petition security interest in rents regardless of whether such an interest would be recognized under state law. *Virginia Beach* fails to follow the rule mandated by this Court in *Butner.*

As *Virginia Beach* is now controlling precedent in the Tenth Circuit, an Oklahoma litigant faces a different result in state and bankruptcy court. Thus, not only does *Virginia Beach* ignore *Erie*'s reasoning, it operates to defeat *Butner*'s mandate. *Virginia Beach* gives a creditor a "windfall merely by reason of the happenstance of a bankruptcy," and elevates a general creditor's right to rental income to that of a secured position, despite the articulated Oklahoma public policy against such a right.

Moreover, *Virginia Beach* cites no Oklahoma authority for the remedy it fashions creating and perfecting an equitable lien on rents. *Virginia Beach* relies only upon bankruptcy decisions and cases from other states, failing to recognize the legal distinctions unique to Oklahoma.

CONCLUSION

Last term in *Lopez supra,* this Court recognized that Congress should be restrained when it attempts to expand federalism and usurp the power of the sovereign States. The federal judiciary is likewise subject to the limitations of the Tenth Amendment. At present, however, there is no mandate from this Court to the circuit courts of appeal requiring them to refer uncertain questions of state law to *state* courts. Petitioners urge that such a mechanism be adopted to ensure that federal courts do not through expedience or impatience ignore the rights of litigants and extend federal common law remedies to deprive

citizens of the several States from rights they enjoy in their own state forum. Congress has not enacted legislation, nor has this Court ruled, that bankruptcy laws make uniform the treatment of property interests in rents. The federal district and appellate courts may not fashion a federal remedy in derogation of state law. For these reasons, the Petition for Certiorari should be granted.

Respectfully submitted,

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APPENDIX A — ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT ENTERED JUNE 6, 1995

UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

No. 93-6304

In re: OKC PARTNERS, LTD., doing business as OKC Partners, Ltd., also known as Town & Country/Courtyard Plaza, a Texas limited partnership

Debtor,

MICHAEL B. BIRNIE,

Creditor,

L. B. WINDHAM; JOHN WINDHAM PLOTNIK; FRED A. SHERIFF; JAY W. LORCH, JOHN H. LINDSEY; DALE B. ELMORE; C. JACKSON GRAYSON, JR.; DOUGLAS A. DAWSON; PETER MARR; HANAHO, LTD.; JOHN J. REDFERN, III; WILLIAM E. PENLAND; EAGLE-TEXAS REALTY COMPANY, INC.,

Appellants,

v.

OKC PARTNERS, LTD.; FIRST GILBRALTER BANK FSB,

Appellees,

Appendix A

and

NORVELL LIPSCOMB, JR. and BLOCKBUSTER VIDEO,

Appellees in the District Court.

ORDER
Entered June 6, 1995

Before SEYMOUR, ALDISERT*, and BALDOCK, Circuit Judges.

This matter come on for consideration of appellants' petition for rehearing and suggestion for rehearing in banc.

Upon consideration whereof, the petition for rehearing is denied by the panel that rendered the decision.

In accordance with Rule 35(b), Federal Rules of Appellate Procedure, the suggestion for rehearing in banc was transmitted to all of the judges of the court who are in regular active service. No member of the panel and no judge in regular active service on the court having requested that the court be polled on rehearing in banc, Rule 35, Federal Rules of Appellate Procedure, the suggestion for rehearing in banc is denied.

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* The Honorable Ruggero J. Aldisert of the United States Court of Appeals for the Third Circuit, sitting by designation.

Appendix A

Entered for the Court

PATRICK FISHER, Clerk

s/ Opal A. Carter
By Opal A. Carter
Deputy Clerk

APPENDIX B — ORDER AND JUDGMENT OF THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT FILED MAY 4, 1995

UNITED STATES COURT OF APPEALS

TENTH CIRCUIT

No. 93-6304

(D.C. No. CIV-92-2403-W)
(W.D. Okla.)

In Re:

OKC PARTNERS, LTD., a Texas limited partnership, also known as Town & Country/Courtyard Plaza, doing business as OKC Partners, Ltd.,

Debtor,

MICHAEL B. BIRNIE,

Creditor,

L.B. WINDHAM; JOHN WINDHAM PLOTNIK; FRED A. SHERIFF; JAY W. LORCH; JOHN H. LINDSEY, DALE B. ELMORE; C. JACKSON GRAYSON, JR.; DOUGLAS A. DAWSON; PETER MARR; HANAHO, LTD.; JOHN J. REDFERN, III; WILLIAM E. PENLAND; EAGLE-TEXAS REALTY COMPANY, INC.,

Appellants,

Appendix B

v.

OKC PARTNERS, LTD., a Texas limited partnership, also known as Town & Country/Courtyard Plaza, doing business as OKC Partners, Ltd.; FIRST GILBRALTER BANK FSB; AMERICAN REINSURANCE COMPANY,

Appellees,

and

NORVELL LIPSCOMB, JR.; and BLOCKBUSTER VIDEO,

Appellees in District Court.

ORDER AND JUDGMENT*

Before **SEYMOUR**, Chief Judge, **ALDISERT**,** and **BALDOCK**, Circuit Judges.

The limited partners of OKC Partners, Ltd., appeal a ruling by the district court that American Reinsurance Company and First Gibralter Bank, F.S.B., had valid liens on the rental income of properties owned by OKC Partners. In affirming the order of

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* This order and judgment is not binding precedent, except under the doctrines of law of the case, res judicata, and collateral estoppel. The court generally disfavors the citation of orders and judgments; nevertheless, an order and judgment may be cited under the terms and conditions of the court's General Order filed November 29, 1993. 151 F.R.D. 470.

** The Honorable Ruggero J. Aldisert, Senior Judge, United States Court of Appeals for the Third Circuit, sitting by designation.

the bankruptcy court, the district court held that our decision in *Virginia Beach Fed. Sav. & Loan Ass'n v. Wood*, 901 F.2d 849 (10th Cir. 1990), is controlling. We agree. After consideration of the record and the parties' arguments, we AFFIRM substantially for the reasons stated in the district court opinion.

Entered for the Court

Stephanie K. Seymour
Chief Judge

APPENDIX C — ORDER OF THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF OKLAHOMA FILED JULY 30, 1993

IN THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF OKLAHOMA

No. CIV-92-2403-W

IN RE:

OKC PARTNERS, LTD., a Texas limited partnership a/k/a TOWN & COUNTRY/COURTYARD PLAZA d/b/a OKC PARTNERS, LTD.,

Debtors.

ORDER

This matter comes before the Court upon the appeal of Appellant, OKC Partners, Ltd. ("OKC Partners"), from the October 21, 1992 Order of the Bankruptcy Court (1) granting Appellee, First Gibraltar F.S.A.'s Motion to Reconsider, (2) vacating the April 25, 1990 Order Dividing Rents, (3) vacating the July 25, 1991 Order Granting Motions to Reconsider and (4) apportioning rental income between Appellee, American Reinsurance Company ("Aetna"), and Appellee, First Gibraltar, F.S.A. ("Gibraltar"). Aetna and Gibraltar have responded to the appeal and OKC Partners has replied thereto. Upon consideration of the parties' submissions, the Court makes its determination.

Background

1. During August of 1983, Town & Country Associates executed a non-recourse promissory note in the principal amount

of $3,600,000.00 in favor of Aetna. The note was secured by a mortgage upon Town & Country Village Shopping Center ("Town & Country") and by an assignment of rents and leases from Town & Country.

2. On June 19, 1985, OKC Partners acquired Town & Country and Courtyard Plaza Shopping Center ("Courtyard"). The acquisition of Town & Country was financed through the assumption of the note and mortgage to Aetna. It was also financed by OKC Partners' execution of a recourse promissory note in the principal amount of $1,000,000.00 and a non-recourse promissory note in the principal amount of $400,000.00 in favor of First Texas Savings & Loan Association ("First Texas"). The notes to First Texas were secured by a second mortgage upon Town & Country. The mortgage included an assignment of rents from Town & Country.

3. OKC Partners' purchase of Courtyard was financed through a recourse promissory note in the principle amount of $805,000.00 and a non-recourse note in the principle amount of $3,220,000.00 made payable to First Texas. The notes were secured by a first mortgage upon Courtyard. The mortgage also included an assignment of rents.

4. On March 30, 1988, First Texas commenced an action to foreclose its second mortgage on Town & Country, to foreclose its first mortgage on Courtyard and to collect the recourse portion of its debt. Shortly after the action was commenced, First Texas filed an application for the appointment of a receiver. Prior to the scheduled hearing, OKC Partners filed for relief under Chapter 11 of the Bankruptcy Code.[1]

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1. To date, Gibraltar has not obtained a judgment in the foreclosure action.

Appendix C

5. On June 6, 1988, First Texas filed a motion with the Bankruptcy Court objecting to the use of its cash collateral (rental income from the shopping centers) by OKC Partners. Subsequently, on August 15, 1988, Aetna also filed with the Bankruptcy Court a notice of its claim under 11 U.S.C. § 546(b) to cash collateral in the form of rents from Town & Country.

6. On September 30, 1993, the Bankruptcy Court modified the automatic stay to permit Aetna and First Texas to proceed with foreclosure of their mortgages. Aetna thereafter commenced its mortgage foreclosure suit.

7. On October 21, 1988, OKC Partners and its general partner filed a motion with the Bankruptcy Court seeking a determination as to the validity of Aetna and First Texas' claims to post-petition rents on the mortgaged premises.

8. On December 27, 1988, First Texas was declared insolvent. Substantially all of First Texas' assets, including the notes at issue, were acquired by Gibraltar.

9. Aetna obtained a foreclosure judgment on September 12, 1989. Town & Country was purchased by Aetna at a sheriff's sale on March 6, 1990. The sale was confirmed on March 23, 1990.

10. On April 25, 1990, the Bankruptcy Court entered an Order dividing post-petition rental income between Aetna and Gibraltar. In awarding rental income, the Bankruptcy Court relied upon the Tenth Circuit's decision in *Virginia Beach Federal Sav. & Loan Ass'n v. Wood,* 901 F.2d 849 (10th Cir. 1990). The Tenth Circuit, in that decision, ruled that a mortgage creates an equitable lien upon rental income and that the equitable lien constitutes the security interest under 11 U.S.C. § 552(b)

which causes rental income to be categorized as cash collateral under 11 U.S.C. § 363(a). In addition, the Tenth Circuit determined that the equitable lien on rental income is perfected by the filing of a § 546(b) claim to cash collateral, which in the Court's view is tantamount to an appointment of a receiver under Oklahoma law. It further concluded that the perfection of the equitable lien relates back to the execution of the mortgage for purposes of § 546(b), but actual entitlement to rental income only relates back to the filing of the § 546(b) notice.

11. Based upon *Virginia Beach*, the Bankruptcy Court awarded Gibraltar post-petition rents from Courtyard from June 6, 1988 and post-petition rents from Town & Country from June 6, 1988 (the date First Texas filed its motion in regard to cash collateral) to August 14, 1988 (the date before Aetna filed its § 546(b) notice). The Bankruptcy Court also awarded Aetna post-petition rents from Town & Country from August 15, 1988 (the date Aetna filed its § 546(b) notice) to March 23, 1990 (the date Town & Country's sale was confirmed).

12. The parties filed motions to reconsider the Bankruptcy Court's Order. On July 25, 1993, the Bankruptcy Court issued an Order granting the motions to reconsider and vacating the April 25, 1990 Order. The Bankruptcy Court determined that the filing of a § 546(b) notice only constitutes perfection of an interest in rental income when a foreclosure judgment has been obtained on the mortgage debt. The Bankruptcy Court concluded that without a foreclosure judgment, there is no assurance that a state court judge would exercise his discretion and order the appointment of a receiver under Oklahoma law. Consequently, the Bankruptcy Court determined that only Aetna had a perfected lien in the rental income and that perfection of the lien occurred on September 12, 1989, the date of its foreclosure judgment. The Bankruptcy Court therefore awarded Aetna rental income from September 12, 1989.

Appendix C

13. Gibraltar filed a motion to reconsider the Bankruptcy Court's Order. On October 21, 1992, the Bankruptcy Court vacated its prior orders and relying upon *Virginia Beach* and the decision of Judge David L. Russell in *Roberts, Gray, Goresen & Moriarty, P.C. v. Resolution Trust Corp. (In re Western Capital Indus., Inc.)*, CIV-90-741-R, Slip. op. (W.D. Okla. October 12, 1990), ruled that Aetna and Gibraltar had equitable liens which were perfected by the filing of the § 546(b) notices. The Court also determined that Aetna was entitled to rent from the date of Gibraltar's § 546(b) notice, June 6, 1988, on the basis that Gibraltar specifically subordinated its interest in the Town & Country rents to Aetna's interest. OKC Partners appealed.[2]

Standard of Review

In reviewing a decision from a bankruptcy court, the district court applies a *de novo* standard of review for legal determinations and a clearly erroneous standard of review for factual findings. *Bartmann v. Maverick Tube Corp.*, 853 F.2d 1540, 1543 (10th Cir. 1988).

Discussion

In this appeal, OKC Partners argues that the Bankruptcy Court erroneously followed the Tenth Circuit's decision in *Virginia Beach* in holding that Aetna and Gibraltar had valid liens

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2. In its Answer Brief, Gibraltar challenges the Bankruptcy Court's ruling in regard to the validity of its assignment of rents and the subordination of its claim to Town & Country rents. The Court has previously granted a motion to strike in relation to the subordination issue. As to the assignment of rents issue, the Court likewise declines to address Gibraltar's challenge since Gibraltar has not appealed the issue and the issue is not properly before the Court.

on the rental income of Town & Country and Courtyard, despite invalid assignments of rents. OKC Partners contends that the *Virginia Beach* decision is contrary to Oklahoma law, especially in light of the Oklahoma Supreme Court's decision in *Teachers Insurance and Annuity Association of America v. Oklahoma Tower Associates Limited Partnership*, 798 F.2d 618 (Okla. 1990). Therefore, OKC Partners contends that *Virginia Beach* should be limited to the facts in that case.

Aetna and Gibraltar contend that the Bankruptcy Court correctly applied *Virginia Beach* in this case. They argue that Oklahoma courts have recognized that a mortgage creates a lien upon rental income. Aetna and Gibraltar therefore argue that *Virginia Beach* is consistent with Oklahoma law and that the Bankruptcy Court correctly concluded that the rental income collected from Town & Country and Courtyard constitute cash collateral securing Aetna and Gibraltar's claims.

In the Court's view, *Virginia Beach* is controlling in this matter. The Court concludes that it is consistent with Oklahoma law and has not been brought into question by the Oklahoma Supreme Court's decision in *Teachers*. In *Teachers*, the mortgagor relied upon *Virginia Beach* and *In re Norman Partners*, 90-146844 Bk-89-4301-LN, Slip. op. (Bankr.W.D.Okla. August 9, 1988), to argue that the mortgagee who had a valid rent assignment had to obtain possession of the mortgage property or an appointment of a receiver to be entitled to rental income from the property. The Oklahoma Supreme Court disagreed, holding that the mortgagee was entitled to all rents collected not only by the receiver but also by the mortgagor. According to the Oklahoma Supreme Court, neither possession of the property nor an appointment of a receiver was necessary when a valid rent assignment existed. The Oklahoma Supreme Court noted the

mortgagor's reliance upon *Virginia Beach* and *In re Norman Partners* but stated that Virginia Beach involved a pre-1986 mortgage and that *Virginia Beach* and *In re Norman Partners* involved a determination of priority of creditors. The Oklahoma Supreme Court rejected the ruling in *In re Norman Partners* to the extent it was inconsistent with the Oklahoma Supreme Court's ruling. However, it did specifically not reject *Virginia Beach.* Because the Oklahoma Supreme Court in *Teachers* did not specifically reject *Virginia Beach*, the Court concludes that the Bankruptcy Court correctly applied it to this case.

In addition, the Court concludes that the Bankruptcy Court correctly relied upon Judge Russell's decision in *Western Capital* in determining that Aetna and Gibraltar had perfected liens upon the filing of the § 546(b) notices. The Court concurs with Judge Russell's finding that the filing of a § 546(b) claim is the legal equivalent to the appointment of a receiver under Oklahoma law and that perfection of an interest in rental income is not dependent upon a finding of entitlement to the appointment of a receiver.

Next, OKC Partners argues that the Bankruptcy Court erred in awarding rental income from Town & Country to Aetna since Aetna does not have a personal deficiency judgment against OKC Partners and cannot obtain one because of its non-recourse promissory note. OKC Partners contends that Aetna must have a personal deficiency judgment under 12 O.S. § 686 to satisfy its debt from anything other than Town & Country itself. Inasmuch as Aetna agreed in its note to look only to the property to satisfy its debt, OKC Partners contends that Aetna is not entitled to rental income from Town & Country.

Aetna, in response, contends that no deficiency judgment is required to recover rents. Aetna concedes that it agreed to look

solely to the security for the indebtedness owed. However, it contends that under the documents executed by OKC Partners and by operation of law, the rents collected from Town & Country were part of the security. According to Aetna, the enforcement of its lien on the rents is not precluded by the limited recourse provisions of the note.

The Court concludes that a personal deficiency judgment is not required for Aetna to be awarded rental income. The mortgage created a lien which attached to rental income. In pursuing its claim to the rents, Aetna was simply enforcing that lien. It was not seeking to execute upon OKC Partners' unencumbered assets. Aetna thus was not required to obtain a personal deficiency judgment. Indeed, this has been the decision of a majority of courts addressing the issue. *See e.g., Prudential Ins. Co. v. Fifty Assoc.,* 503 F.2d 925 (9th Cir. 1974); *Hatch v. Security-First Nat'l Bank,* 120 P.2d 869 (Cal. 1942); *Smith v. Mutual Ben. Life Ins. Co.,* 106 N.W.2d 515 (Mich. 1960); *Metropolitan Life Ins. Co. v. Rosenfield,* 274 N.Y.S. 531 (N.Y.Sup. 1934). Therefore, the Bankruptcy Court did not err in awarding rental income from Town & Country to Aetna.

In addition, OKC Partners argues that the Bankruptcy Court erred in awarding Gibraltar rental income as a judgment has never been entered in the foreclosure proceedings commenced by Gibraltar. OKC Partners argues that until a judgment has been entered, Gibraltar should not be awarded any rents from Courtyard.

Gibraltar, in response, contends that under *Virginia Beach,* it is entitled to rents at the time it filed its § 546(b) notice. Thus, Gibraltar argues that it is not required to obtain a judgment to be awarded rents.

Appendix C

The Court concludes that Gibraltar has a perfected lien in the rental income under *Virginia Beach* and is entitled to rents from the date of the filing of its § 546(b) claim. However, the Court also concludes that Gibraltar is not entitled to distribution of the rents until a judgment is entered in favor of Gibraltar in the foreclosure proceedings. A § 546(b) notice is equivalent to the appointment of a receiver under Oklahoma law. As the Oklahoma Supreme Court recognized in *Rives v. Mincks Hotel Co.*, 30 P.2d 911, 915 (Okla. 1934), when a receiver is appointed, the receiver holds the proceeds until such time as a court makes "proper orders for the distribution of funs in accordance with the rights of the various parties." The Court thus concludes that Gibraltar, although entitled to rental income by virtue of its lien, is not entitled to receive the rental income until a judgment in the foreclosure action has been entered. The rental income should stay in the cash collateral account of OKC Partners until judgment is entered.

Conclusion

Based upon the foregoing, the Bankruptcy Court's Order of October 21, 1992 is AFFIRMED to the extent that Aetna and Gibraltar are entitled to rents from Town & Country and Courtyard and is REVERSED to the extent that it infers that Gibraltar is entitled to distribution of the rents prior to entry of judgment in the foreclosure action.

ENTERED this 30th day of July, 1993.

s/ Lee R. West
LEE R. WEST
UNITED STATES DISTRICT JUDGE
ENTERED IN JUDGEMENT DOCKET ON 7-30-93

APPENDIX D — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT FILED APRIL 18, 1990

VIRGINIA BEACH FEDERAL SAVINGS AND LOAN ASSOCIATION,
Plaintiff-Appellee,

v.

Frank E. WOOD; Beverly J. Wood, doing business as Franklin Investments, Franklin Development Co., and Franklin Woodworks; Frank E. Wood; Beverly J. Wood, and the Unsecured Creditors Committee (UCC),
Defendants-Appellants.

No. 88-1308.

United States Court of Appeals,
Tenth Circuit.

April 18, 1990.

* * *

James A. Hogue, Sr., Hogue and Turkel, Inc., Tulsa, Okl., for defendants-appellants.

Andrew R. Turner, Conner & Winters, Tulsa, Okl., for plaintiff-appellee.

Before TACHA, BALDOCK, and BRORBY, Circuit Judges.

PER CURIAM

After examining the briefs and appellate record, this panel has determined unanimously that oral argument would not materially assist the determination of this appeal. *See*

Fed.R.App.P. 34(a); 10th Cir.R. 34.1.9. The case is therefore ordered submitted without oral argument.

During March of 1983, appellants Frank and Beverly Wood (hereinafter debtors)[1] executed an installment note in the principal amount of $1,500,000.00 in favor of First City Mortgage Company. This note was almost immediately assigned to appellee Virginia Beach Federal Savings and Loan Association (hereinafter VBF). The note was secured by a mortgage and security agreement as well as an assignment of interest in leases, all executed by debtors in favor of First City and then assigned to VBF.

Debtors defaulted on the note leaving an unpaid balance of approximately $1,500,000.00 including interest. VBF commenced a foreclosure action in state court in an effort to obtain the premises that were mortgaged to secure the debt. The state court entered a journal entry of judgment in favor of VBF which included an order of foreclosure authorizing a sheriff's sale. VBF did not seek the appointment of a receiver pending the sale.

The sale was stayed by debtors' filing of a petition for relief under Chapter 11 of the Bankruptcy Code. In the bankruptcy court, VBF filed a notice of its claim under 11 U.S.C. § 546(b) to cash collateral in the form of rental income from the mortgaged property. The bankruptcy court denied VBF's claim. VBF appealed to the district court. The district court reversed and held that VBF was entitled to the rental income since the filing of the § 546(b) notice. 97 B.R. 71.

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1. For the purposes of this opinion, we subsume within the term "debtors" appellant unsecured creditors committee — a party of like interest to the Woods.

Appendix D

On appeal, debtors essentially make two assignments of district court error. First, debtors contend that the district court erred in its legal conclusion that VBF was entitled to the rental income. Second, debtors argue that the district court erred procedurally by permitting a magistrate to conduct an advisory hearing and that the bankruptcy appeal was actually decided by a magistrate and not by an Article III judge. For the reasons set forth below, we affirm.

In reviewing the decision of a bankruptcy court, the district court and the court of appeals apply the same standards of review—*de novo* for legal determinations and clearly erroneous for factual findings — that govern the appellate review in other cases. *See, e.g., Bartmann v. Maverick Tube Corp.*, 853 F.2d 1540,1543 (10th Cir. 1988).

Initially, we determine that debtors' second appellate argument is without merit. We agree with debtors that magistrates are not permitted to enter final decisions in bankruptcy appeals. However, there is no evidence that that was done in this case. The final order which we now review was signed by the district judge.

Turning to debtors' first appellate argument, we must begin by determining whether the subject rental income can be considered cash collateral under the Bankruptcy Code. Cash collateral is defined by 11 U.S.C. § 363(a).[2] Rental income from

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2. Cash collateral is defined in 11 U.S.C. § 363(a) as follows:

> In this section, "cash collateral" means cash, negotiable instruments, documents of title, securities, deposit accounts, or other cash equivalents whenever acquired in which the estate and an entity other than the estate have an interest and includes the proceeds,

(Cont'd)

property subject to a security interest as provided for in 11 U.S.C. § 552(b)[3] comes within the definition of cash collateral. We look to state law to determine whether VBF had the requisite security interest in the subject rental income. *See Butner v. United States,* 440 U.S. 48, 55-57, 99 S.Ct. 914, 918-19, 59 L.Ed.2d 136 (1979).

VBF does not ground its security interest on the assignment of interest in leases. It concedes that such an assignment of rental income made conditional upon the future default of the mortgagor was void and unenforceable during the time period relevant to this case.[4] *See Hart v. Bingman,* 171 Okla. 429, 43 P.2d 447, 449 (1935) (holding mortgage clauses which attempt to pledge rents to be void and unenforceable because they are contrary to public policy).

(Cont'd)

> products, offspring, rents, or profits of property subject to a security interest as provided in section 552(b) of this title, whether existing before or after the commencement of a case under this title.

3. 11 U.S.C. § 552(b) reads as follows:

Except as provided in sections 363, 506(c), 522, 544, 545, 547, and 548 of this title, if the debtor and an entity entered into a security agreement before the commencement of the case and if the security interest created by such security agreement extends to property of the debtor acquired before the commencement of the case and to proceeds, product, offspring, rents, or profits of such property, then such security interest extends to such proceeds, product, offspring, rents, or profits acquired by the estate after the commencement of the case to the extent provided by such security agreement and by applicable nonbankruptcy law, except to any extent that the court, after notice and a hearing and based on the equities of the case, orders otherwise.

4. Oklahoma law presently permits the enforceability of such assignments of rental income. *See* Okla.Stat. tit. 46 § 4 (effective Nov. 1, 1986). This new law is not retroactive and has no effect on the outcome of this case.

VBF's claim to the rental income stems from the existence of the mortgage itself. This court, in reliance upon the language of the state statute governing the appointment of a receiver, Okla.Stat. § 518(2) (1921) (predecessor provision to identical Okla.Stat. tit. 12, § 1551(2)(1981)) (since amended, effective Nov. 1, 1989), stated "[t]he statute recognizes the mortgage as creating an equitable lien on the rents pending foreclosure." *Little v. Keaton,* 38 F.2d 457, 461 (10th Cir.), *cert. denied,* 282 U.S. 847, 51 S.Ct. 26, 75 L.Ed. 751 (1930). This equitable lien arising from the mortgage and security agreement constitutes the security interest under § 552(b) that causes the rental income to be categorized as cash collateral under § 363(a).

Section 552(b) qualifies the continuing (postpetition) force of a prepetition security interest by noting the overarching control of other code sections, including 11 U.S.C.§ 544.[5] Section

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5. 11 U.S.C. § 544(a) reads as follows:

The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by—

> (1) a creditor that extends credit to the debtor at the time of the commencement of the case, and that obtains, at such time and with respect to such credit, a judicial lien on all property on which a creditor on a simple contract could have obtained such a judicial lien, whether or not such a creditor exists;
>
> (2) a creditor that extends credit to the debtor at the time of the commencement of the case, and obtains, at such time and with respect to such credit, an execution

(Cont'd)

544(a) provides that, upon the commencement of a bankruptcy case, a trustee (or, as in the instant case, a debtor-in-possession, *see* 11 U.S.C. § 1107(a)) has the rights and powers of both a hypothetical judicial lien creditor and a bona fide purchaser to avoid any transfer of the debtor's property if the conveyed interest was not perfected prepetition.

State law controls the issue of whether a property interest has been perfected. *See Butner,* 440 U.S. at 55, 99 S.Ct. at 918. Oklahoma is a lien theory state. *See Hart,* 43 P.2d at 449. Thus, the mortgagor remains the legal owner of the mortgaged property. *See Coursey v. Fairchild,* 436 P.2d 35, 38 (1967). The right of possession to the property (and, incidentally, to the rental income derived therefrom) "is dependent wholly upon the termination of a foreclosure action, except as to the statutory and equitable powers relating to the appointment of a receiver." *Hart,* 43 P.2d at 449. Although the Oklahoma courts have not written in terms of "perfection" of the interest of a mortgagee in the rental income drawn from the mortgaged premises, it is clear that, for purposes of this case, perfection is equivalent to the present right to receive the rental income. Therefore, a mortgagee perfects its interest when it either properly obtains possession of the property or obtains the appointment of a receiver.

VBF neither obtained possession of the property nor the

(Cont'd)

against the debtor that is returned unsatisfied at such time, whether or not such a creditor exists; or

(3) a bona fide purchaser of real property, other than fixtures, from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser and has perfected such transfer at the time of the commencement of the case, whether or not such a purchaser exists.

appointment of a receiver prior to debtors filing their bankruptcy petition. Although it would appear, without more, that § 544(a) would permit debtors to retain the subject rental income, the Fifth Circuit has correctly stated the following:

> The starting point to determine whether 11 U.S.C. § 544(a)(1) or (3) prevents the postpetition perfection of a security interest in rents is 11 U.S.C. § 362(a)(4). Under 362(a)(4), any act to perfect any lien against property of the estate is stayed by the filing of a bankruptcy petition under 11 U.S.C. §§ 301-303. An exception to § 362(a)(4) exists, though, for acts taken "to perfect an interest in property to the extent that the trustee's rights and powers are subject to such perfection under" 11 U.S.C. § 546(b). 11 U.S.C. § 362(b)(3). Section 546(b) limits a trustee's § 544 avoiding powers if generally applicable law "permits perfection of an interest in property to be effective against an entity that acquires rights" in the property before the date of perfection. If that law requires that the property be seized or that an action be commenced to perfect the security interest and that action was not taken before the bankruptcy petition was filed, the interest is perfected by postpetition notice. 11 U.S.C. § 546(b).
>
> For [the mortgagee] to escape having its [security interest in the rental income] voided under § 544(a), [state] law must permit a

> creditor such as [the mortgagee] to enforce a security interest in rents against an entity that acquired rights to the rents before the creditor perfected. That is, [state] law must authorize the creditor's perfection to relate back to a time before [the debtor] filed his bankruptcy petition and, as a debtor-in-possession, assumed the status of a lien creditor or bona fide purchaser.

In re Casbeer, 793 F.2d 1436, 1442-43 (5th Cir.1986) (footnotes omitted).

At the time of the commencement of the bankruptcy case, VBF was entitled, under Oklahoma law, to have a receiver appointed, and to obtain the rental income that accrued from that point forward. VBF did not move to have a receiver appointed because of the relatively quick setting of the sheriff's sale by which it anticipated acquiring of property outright. Okla.Stat. tit. 12, § 1551(2) requires the mortgagee to demonstrate that the mortgaged property is in danger of being lost, removed, or materially injured or that the condition of the mortgage has not been performed and that the property is probably insufficient to discharge the mortgage debt. There is no dispute in this case that the installment notice is in default and that the value of the mortgaged property (approximately $1,250,000.00) was significantly below the amount of the outstanding indebtedness at the time the district court order was entered (approximately $1,700,000.00). Had VBF sought the prepetition appointment of a receiver under § 1551(2), VBF would have perfected its interest in the rental income.

VBF contends that its § 546(b) notice of claim to cash

collateral is tantamount to a motion for the appointment of a receiver under Okla.Stat. tit. 12, § 1551(2) to which VBF would, absent the bankruptcy proceedings, be entitled to file. VBF asserts that this notice perfected its interest in the rental income and that this perfection related back to a prepetition time. This assertion is correct.

By its nature, the equitable lien on the rental income possessed by VBF relates back to a prepetition time, specifically, the time that the mortgage was executed.

> An equitable lien is a mere floating equity until a judgment or decree subjecting the property to the payment of a debt or claim is rendered, but even though not judicially recognized until a judgment declaring its existence, it relates back to the time it was created by the conduct of the parties.

51 Am.Jur.2d *Liens* § 22 (1970). *See also In re Stratton,* 106 B.R. 188, 193 (Bankr.E. D.Cal.1989); *Matter of Adametz,* 53 B.R. 299, 307 (Bankr.W.D.Wis.1985); *United States through Farmers Home Admin. v. Redland,* 695 P.2d 1031, 1040 (Wyo.1985). *Accord Leyden v. Citicorp Indus. Bank,* 782 P.2d 6, 11 n. 10 (Colo.1989).

Although the perfection of VBF's interest in the rents relates back to the time of the execution of the mortgage for the purpose of § 546(b), the entitlement to the rental income does not relate back. Under Oklahoma law, a mortgagee is not entitled to recover the rental income prior to the appointment or recognition of a receiver. *See Hart,* 43 P.2d at 451. VBF's § 546(b) notice serves as the federal bankruptcy equivalent of the appointment or

recognition of a receiver under Oklahoma law. VBF is entitled to the rental income from the subject property from that time forward. Furthermore, as the Fifth Circuit observed in *Casbeer,* 793 F.2d at 1443, this result comports with the direction in *Butner* that state law should be applied in determining the exact extent of a mortgagee's interest in rental income. This uniform application of state and federal law in this regard prevents "a party from receiving 'a windfall merely by reason of the happenstance of bankruptcy.' " *Butner,* 440 U.S. at 55, 99 S.Ct. at 918 *quoting Lewis v. Manufacturers Nat'l Bank,* 364 U.S. 603, 609, 81 S.Ct. 347, 350, 5 L.Ed.2d 323 (1961).

The judgment of the United States District Court for the Northern District of Oklahoma entered on February 19,1988, is AFFIRMED.

Supreme Court, U.S.
FILED
OCT 30 1995
CLERK

(2)

No. 95-195

In the Supreme Court of the United States

OCTOBER TERM, 1995

L.B. WINDHAM, ET AL., PETITIONERS

v.

FIRST GIBRALTAR BANK, F.S.B.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE FEDERAL DEPOSIT INSURANCE CORPORATION IN OPPOSITION

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QUESTION PRESENTED

Whether the court of appeals correctly decided, under Oklahoma law, that a mortgage creates a lien upon the rents and profits collected from mortgaged property, for purposes of determining whether a mortgage holder's lien on rents and profits has been perfected in accordance with 11 U.S.C. 546(b).

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 4a-6a) is unpublished, but the decision is noted at 53 F.3d 342 (Table). The opinions of the district court (Pet. App. 7a-15a) and the bankruptcy court are unreported.

JURISDICTION

The judgment of the court of appeals was entered on May 4, 1995. A petition for rehearing was denied on June 6, 1995. Pet. App. 2a-3a. The petition for a writ of certiorari was filed on August 3, 1995. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioners are limited partners and the general partner of OKC Partners, Ltd., a Texas limited partnership (the Partnership). Pet. 3. In 1985, the Partnership mortgaged two shopping centers to First Texas Savings & Loan Association. *Ibid.*; Pet. App. 8a.[1]

2. On March 30, 1988, First Texas commenced an action in an Oklahoma state court to foreclose on its mortgages and to collect the recourse portion of its debt. Shortly after the action was commenced, First Texas filed an application for the appointment of a receiver. Pet. 5; Pet. App. 8a. On May 24, 1988, the Partnership filed for relief under Chapter 11 of the Bankruptcy Code in the United States Bankruptcy Court for the Western District of Oklahoma. Pet. 5.

3. On June 6, 1988, First Texas filed a motion with the bankruptcy court objecting to the debtor's use of rents from the shopping centers and seeking to modify the automatic stay. While the motion was pending before the bankruptcy court, First Texas was declared insolvent, and the notes and mortgages that are the subject of this litigation were acquired by First Gibraltar Bank (Gibraltar), F.S.B.[2] Pet. App. 9a; Pet. 5.

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[1] One of the shopping centers, Town & Country Village Shopping Center, was subject to a prior mortgage lien in favor of American Reinsurance Company. Pet. App. 7a-8a. American Reinsurance was a party in this case in the court of appeals.

[2] On June 16, 1995, following the court of appeals' decision and issuance of the mandate, the Federal Deposit Insurance Corporation as Manager of the FSLIC Resolution Fund entered into an agreement with First Nationwide Bank, A

4. On October 21, 1992, after reconsidering and vacating its prior orders, the bankruptcy court entered an order holding that, under Oklahoma law, the mortgages created a lien upon the rents and profits from the shopping centers. The bankruptcy court further held that Gibraltar's lien had been perfected by the filing of First Texas' motion objecting to the debtors' use of rents from the shopping centers, which constituted a notice under Section 546(b) of the Bankruptcy Code, 11 U.S.C. 546(b).[3] Pet. App. 11a.

Federal Savings Bank, the successor to First Gibraltar Bank, F.S.B. Under that agreement, the notes and mortgages subject to this litigation were transferred to the FDIC, effective June 1, 1995. We have filed a motion in this Court requesting the substitution of the FDIC for Gibraltar as the respondent in this case. To avoid confusion, Gibraltar is referred to herein as the respondent.

[3] Section 546(b), at all times relevant hereto, stated:

> The rights and powers of a trustee under section[s] 544, 545, and 549 of this title are subject to any generally applicable law that permits perfection of an interest in property to be effective against an entity that acquires rights in such property before the date of such perfection. If such law requires seizure of such property or commencement of an action to accomplish such perfection, and such property has not been seized or such action has not been commenced before the date of the filing of the petition, such interest in such property shall be perfected by notice within the time fixed by such law for such seizure or commencement.

11 U.S.C. 546(b) (Supp. III 1979). Under Section 546(b), a mortgage lien holder is permitted to perfect its lien in rents following the filing of a bankruptcy petition if, under applicable state law, perfection could relate back to defeat the rights of an intervening creditor. In addition, if applicable state law requires seizure or the commencement of a legal

5. On appeal, the district court affirmed the bankruptcy court. Pet. App. 15a.[4] The district court held that the outcome of the case was controlled by the Tenth Circuit's decision in *Virginia Beach Fed. Sav. & Loan Ass'n* v. *Wood*, 901 F.2d 849 (10th Cir. 1990). In the district court's view, the Tenth Circuit's decision in that case, which arose in a similar context and also involved the application of Oklahoma law, was "consistent with Oklahoma law" and had "not been brought into question" by a subsequent Oklahoma decision, *Teachers Ins. & Annuity Ass'n* v. *Oklahoma Tower Associates Ltd. Partnership*, 798 P.2d 618 (Okla. 1990). Pet. App. 12a.

6. The court of appeals affirmed in an unpublished order. Pet. App. 4a-6a. The court of appeals stated that its decision in *Virginia Beach* was controlling, and it affirmed "substantially for the reasons stated in the district court opinion." Pet. App. 6a.

ARGUMENT

Petitioners claim that the courts below did not apply Oklahoma law to determine whether Gibraltar's mortgage liens extended to rents and profits from the

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action to accomplish perfection, a motion filed in accordance with Section 546(b) will be sufficient to perfect the lien. 4 *Collier on Bankruptcy* ¶ 546.03 (L. King ed., 15th ed. 1995).

In 1994, Section 546(b) was amended to make clear that it was applicable to acts to continue or maintain perfection in property. The amendment is effective in bankruptcy cases filed on or after October 22, 1994. *Collier on Bankruptcy, supra*, ¶ 546.03, n.a.; Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, §§ 204, 702, 108 Stat. 4122, 4150.

[4] The district court reversed the bankruptcy court on the limited issue of the timing of the distribution of the rents to Gibraltar. Pet. App. 15a. The instant petition does not raise any issue regarding that holding.

shopping centers and that, insofar as they did apply Oklahoma law, they did so incorrectly. The alleged conflict with state law would not provide a sufficient basis upon which to grant certiorari and, in any event, no such conflict exists.

1. Petitioners claim (Pet. 6-10) that the courts below did not apply Oklahoma law in determining whether Gibraltar's mortgage liens extended to rents and profits from the shopping centers. To the contrary, the Tenth Circuit in *Virginia Beach* expressly applied state law in a similar context, the district court in this case re-examined and reaffirmed the *Virginia Beach* result in light of a later state law precedent, and the court of appeals in this case again re-examined the issue and again reached the same conclusion.

a. Relying upon this Court's decision in *Butner* v. *United States*, 440 U.S. 48, 55-57 (1979),[5] the Tenth Circuit in *Virginia Beach* made quite clear that it "look[s] to state law to determine whether [the mortgagee] had the requisite security interest in the subject rental income," 901 F.2d at 851; Pet. App. 19a, and that "[s]tate law controls the issue of whether a property interest has been perfected." 901 F.2d at

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[5] At issue in *Butner* was whether state or federal law should determine if rents collected by a bankruptcy trustee between the filing of a bankruptcy petition and the foreclosure sale of the property should be applied against the outstanding indebtedness of the second mortgage. This Court ruled that state law governs:

> [T]he federal bankruptcy court should take whatever steps are necessary to ensure that the mortgagee is afforded in federal bankruptcy court the same protection he would have under state law if no bankruptcy had ensued.

440 U.S. at 56.

852; Pet. App. 21a. After reviewing Oklahoma statutory and case law, the court held that a mortgagee may obtain such a security interest under Oklahoma law and that it is perfected when the mortgagee either seizes the property or obtains the appointment of a receiver. 901 F.2d at 851-852; Pet. App. 20a-21a. Based on that premise, the court held that a mortgage holder perfects its lien on rent by filing a notice under Section 546(b). 901 F.2d at 852; Pet. App. 22a-23a. The court of appeals concluded by stating:

> [T]his result comports with the direction in *Butner* that state law should be applied in determining the exact extent of a mortgagee's interest in rental income.

901 F.2d at 853; Pet. App. 25a. The decision in *Virginia Beach* was thus expressly based upon state law.

b. In this case, the district court carefully considered petitioners' claim that the *Virginia Beach* decision had misread Oklahoma law. The court reviewed the decision in *Virginia Beach* and considered whether an intervening state law precedent cited by petitioners cast any light on the continuing validity of the *Virginia Beach* holding. Pet. App. 12a-13a. The district court noted that the Oklahoma Supreme Court "specifically [did] not reject *Virginia Beach*" in the later case, but instead distinguished it on the ground that it involved a mortgage that, like the mortgage at issue in this case, was entered into under a prior statute. Pet. App. 13a. The court concluded that *Virginia Beach* "is controlling in this matter," that it "is consistent with Oklahoma law," and that it "has not been brought into question" by the later Oklahoma decision. Pet. App. 12a.

c. The court of appeals affirmed the district court's holding for the reasons given in the district court's opinion. The fact that the court of appeals found it unnecessary to restate the district court's sound reasoning in its own words does not suggest any error concerning the applicable source of law; the court had made quite clear in *Virginia Beach* its understanding that state law controlled. And although petitioners appear to contend (Pet. 10-11) that the court of appeals' failure to write an opinion suggests that it did not review the district court's conclusions concerning state law under the appropriate *de novo* standard, see *Salve Regina College* v. *Russell*, 499 U.S. 225, 231 (1991), the only support for that conclusion is petitioners' own unsupported speculation.

2. Petitioners also seek (Pet. 11-12) to impose a requirement that a court of appeals include language in any opinion to the effect that the court has either examined applicable state law and determined that the applicable state law is settled, or that the court is certifying the question to the State's highest court because of uncertainty in the state law. Any such requirement would be unwarranted. Under well-settled jurisprudence, the court of appeals had broad discretion to determine that certification to the Oklahoma Supreme Court was unnecessary. See *Lehman Bros.* v. *Schein*, 416 U.S. 386, 389-391 (1974); *id.* at 392-395 (Rehnquist, J., concurring). The court of appeals' affirmance reflects a decision that certification was unnecessary.[6]

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[6] The district court denied a motion filed by the Partnership requesting certification to the Supreme Court of Oklahoma of state law questions. In denying the motion, the

3. Petitioners' various claims reduce to the contention that the courts below misapplied state law in this case. Even if petitioners were correct in this contention, a misapplication of state law would provide no basis for further review in this Court. See *Sheridan* v. *United States*, 487 U.S. 392, 401-402 (1988); *Butner*, 440 U.S. at 57-58; *Huddleston* v. *Dwyer*, 322 U.S. 232, 237 (1944).

In any event, the court of appeals correctly applied state law. As the court held in *Virginia Beach*, a mortgage constitutes a lien upon rental income under Oklahoma law. 901 F.2d at 851; Pet. App. 20a. Such a lien can be perfected by foreclosure or by the judicial appointment of a receiver. *Little* v. *Keaton*, 38 F.2d 457, 461 (10th Cir.), cert. denied, 282 U.S. 847 (1930) ("The statute recognizes the mortgage as creating an equitable lien on the rents pending foreclosure."); *Hart* v. *Bingman*, 43 P.2d 447 (Okla. 1935); Okla. Stat. tit. 12, § 1551 (1993).

The sole authorities cited by petitioners in support of their argument to the contrary (Pet. 13), Okla. Stat. tit. 42, §§ 10, 11 (1990),[7] are irrelevant here.

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district court stated: "There is sufficient authority to guide the court in resolving the legal issues presented." District Court Docket No. 11, Order of January 25, 1993.

[7] Title 42 Okla. Stat. §§ 10 and 11 provide:

§ 10. Lien transfers no title.

Notwithstanding an agreement to the contrary, a lien or a contract for a lien transfers no title to the property subject to the lien.

§ 11. Contracts for forfeiture of property and restraining redemption.

All contracts for the forfeiture of property subject to a lien, in satisfaction of the obligation secured thereby, and

Neither provision addresses the creation or perfection of a mortgage holder's lien upon rental income. Under Oklahoma law, the lien interest arises from the mortgage itself, without regard to whether there is an assignment of rents created either by separate instruments or by specific provisions contained in the mortgage document. For that reason, petitioners' references to Oklahoma law regarding the enforceability of an assignment of rents (Pet. 3) have no bearing on the issue in this case.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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OCTOBER 1995

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all contracts in restraint of the right of redemption from a lien, are void, except in the case specified in Section 1122.

Okla. Stat. tit. 42 §§ 10, 11 (1990).